

Auditing the NCUA 5300 Call Report

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Learning Objectives

- Discuss recent changes to the NCUA 5300 call report
- Review key areas in completing the NCUA 5300 call report
- Identify key audit steps in completing an audit of the 5300 call report

Why Audit the Call Report

- Recent changes to call report now includes penalties for late filing
- An increasing number of call report findings presented in examination reports
- A key assessment of management's financial reporting accuracy
- Provides the internal audit department with additional knowledge related to the financial function of the credit union

NCUA 5300 Call Report

- Key information related to the 5300 call report:
 - The Online 5300 Call Report system is used to collect the quarterly financial information of credit unions.
 - The system is real-time, so call reports are available to the public more timely (generally within one week of submission).

NCUA 5300 Call Report

- Accuracy of Information
 - Credit unions more than \$10 Million in total assets must follow generally accepted accounting principles (GAAP), which requires the call report to be prepared in accordance with GAAP.
 - If the credit union has a wholly owned or majority owned (over 50 percent) credit union service organization (CUSO) it must be consolidated for the call report.

Upgrade to CU Online

- Based on credit union feedback, the NCUA launched an upgraded version of CU Online on May 28, 2012. The upgrade was designed to:
 - Improve data integrity
 - ◇ Instant warnings to prevent data-entry errors and omissions and to identify inconsistencies with historical data
 - ◇ Real-time calculations and edits without a need to save changes
 - Enhance security
 - Make CU Online more user-friendly

Call Report Format

Call reports are divided into four areas:

1) Core section (pages 1-10)

- completed by all credit unions

2) PCA Net Worth Calculation Worksheet (page 11)

- Generally, requires no input unless merger activities or using alternative net worth calculation

Call Report Format

Call reports are divided into four areas (continued):

**3) Risk Based Net Worth Requirement Worksheet
(page 12)**

- Automated and requires no input

4) Supplementary schedules (pages 13-25)

- To be completed as applicable

Recent Changes to the Call Report

- 1. NCUA Letter to Credit Unions 13-CU-11**
- 2. NCUA Letter to Credit Unions 14-CU-03**
- 3. Changes effective March 2014**
- 4. Other recent changes**

NCUA Letter to Credit Unions 13-CU-11

- **Call Reports must be filed electronically beginning with the December 2013 Call Report**
- **Paper filing is no longer permitted in order to:**
 - Reduce operating costs
 - Promote environmentally responsible practices
 - Reduce data entry errors
 - Allow NCUA to compile quarterly industry data on a more timely basis
- **Submission due dates extended to the 4th Friday of each month following the end of a quarter**

NCUA Letter to Credit Unions 14-CU-03

Late filings of quarterly Call Report and Profile data have become a serious problem.

Number of late filers has been over 1,000 credit unions of all sizes per Call Report Cycle.

NCUA will begin to exercise its authority to impose civil money penalties against late filers.

All civil money penalties will be remitted to the U.S. Treasury, not retained for NCUA use.

NCUA Letter to Credit Unions 14-CU-03

Penalties will be assessed for each day a required report is late, or contains inaccurate information:

- Up to a maximum of \$2,000 per day for each day a required report is minimally late or contains unintentional errors.
- Up to a maximum of \$20,000 per day for each day a required report is late or contains errors not covered in the first bullet point above.
- Up to a maximum of \$1 million (or 1% of total assets, whichever is less) per day if a FICU knowingly or with reckless disregard for accuracy submits a false or misleading report and fails to correct it.

NCUA Letter to Credit Unions 14-CU-03

When determining the exact amount to be assessed against a FICU, NCUA will consider mitigating factors outlined in Section 206 of the Federal Credit Union Act. These include:

- The size of financial resources and good faith of the credit union
- The gravity of the violation
- The history of previous violations
- Other matters as justice may require regarding the circumstances of late or false/misleading submissions, such as natural disasters, incapacitation of key employees, etc.

NCUA Letter to Credit Unions 14-CU-03

- **Fines are effective with the March 2014 Call Report**
- **NCUA will publish the names of FICUs assessed with civil money penalties.**
- **While the number of credit unions filing Call Reports late for the fourth quarter of 2013 fell by more than two-thirds from the number of late filers at the end of 2012, hundreds of credit unions are still filing late according to the NCUA.**

March 2014 Changes

New Investment Disclosures (page 18)

Amounts reported in the asset section of the statement of financial condition to fund employee benefit or deferred compensation plans (line 20)

Excludes:

- 457b plan assets
- Pension plan assets that do not reside on the credit union's balance sheet
 - 401k plans
 - Defined benefit plans

March 2014 Changes

New Investment Disclosures (continued)

Includes:

Securities (trading, AFS or HTM)

Other investments (other investments disclosed on page 1)

Other assets

- Split dollar arrangements
 - Collateral assignment (the credit union grants a loan to an official to purchase life insurance)
 - Endorsement (the credit union owns the life insurance and endorses some or all of the death benefit)
- Other insurance (non-split dollar insurance policies owned by the credit union)
- Other non-insurance (not reported in any of the categories above)

Investments in charitable donation accounts (line 21)

March 2014 Changes

New Derivative Disclosures

Derivatives include:

- Interest rate swaps – exchange interest rate cash flows (variable for fixed)
- Interest rate options – option to purchase interest rate cap or floor
- Treasury futures
- Others

Extensive and complicated

Call Report pages impacted include:

- Assets (page 2)
- Liabilities (page 3)
- Gains and losses (page 5)
- New Schedule D – Transactions Reports (pages 20-24)

March 2014 Changes

New Schedule D – Derivative Transactions Reports

Section 1 – Outstanding (page 20)

- Transactions outstanding by type

Section 2 – Outstanding with Accounting Designation (page 21)

- Transactions outstanding by accounting designation (no hedge, fair value hedge, and cash flow hedge)

Section 3 – Activity (page 22)

Section 4 – Maturity Horizon (page 23)

Section 5 – Counterparty Exposure (page 24)

March 2014 Changes

New Schedule E – BSA/AML information (page 25)

Includes information concerning accounts provided to Money Services Business (MSBs) as defined by the Financial Crimes Enforcement Network (FinCEN):

- Dealers in foreign exchange
- Check cashers
- Issuers or sellers of traveler's checks or money orders
- Money transmitters
- Providers of prepaid access
- Sellers of prepaid access

Other Recent Changes

Enhanced error checking

Allowance for Loan Loss (ALL) roll-forward (beginning balance, plus provision expense, less charge-offs, plus recoveries) must equal ending ALL balance within +/- \$1,000

Need to consider overdraft protection program activity

Need to consider Collateral in Process of Liquidation (CIPL) mark-to-market adjustments

Other Recent Changes

Delinquent Loans by Collateral Type – Page 7

Loan delinquency reporting now based on number of days (60) vs. number of months (2)

Change aligns reporting with other federal regulators and eliminates confusion arising from differences in the number of days per month

This could result in higher reportable delinquency as several credit unions changed all due dates to the 1st of the month when the new truth in lending disclosure was implemented (length of time between statement date and loan due date)

Other Recent Changes

Liquidity, Commitments and Sources – Page 10

New line items for various sources of lines of credit and borrowed funds outstanding

Schedule A – Specialized Lending – Page 16

New disclosures for Purchased Credit Impaired Loans (PCILs)

This is primarily applicable to credit unions that have purchased impaired loans through merger and acquisition activities

Results of March 2014 Late Filing

Summary Statistics - All Late Filers (March 2014 Cycle)					
Total Late Filers				Days Late	Count
Federally Insured Credit Unions	104			1	21
Late Filers by Charter Type				2	6
Federal Charter	75	72.1%		3	22
Federally Insured, State Charter	29	27.9%		4	20
Late Filing FICUs - By Asset Size				5	11
Minimum Asset Size	\$	44,375		6	6
Under \$1 Million	31	29.8%		7	4
\$1 to \$10 Million	33	31.7%		8	2
\$10 to \$50 Million	29	27.9%		10	4
\$50 to \$250 Million	11	10.6%		11	5
Over \$250 Million	0	0.0%		12	1
Maximum Asset Size	\$	243,375,870		13	1
				22	1
				Total	104

Source: NCUA

Internal Controls Over Call Reporting

- **Internal Control Overview**
- **Credit Union User Roles**
- **Segregation of Duties**
- **Other Internal Control Considerations**

Internal Control Overview

Internal control is defined as a process designed to help the organization accomplish specific goals or objectives through the following:

- organization's structure
- work and authority flows
- people
- management information systems

Internal Control Overview

It is a means by which a credit union's resources are directed, monitored, and measured.

It plays an important role in preventing and detecting fraud and protecting the credit union's resources

- physical (e.g., cash, securities, and property)
- intangible (e.g., reputation, intellectual property, and member loyalty).

Credit Union User Roles

All users of the Credit Union Online system must be registered and assigned one of two credit union user roles:

1. **Credit Union Administrator**
2. **Credit Union User**

Credit Union Administrator

There must be at least two administrators. However, the total number should be limited. administrators have the ability to:

- Add, edit, and delete users
- Reset passwords and unlock user accounts
- Resend account verification emails for users
- Change their personal information
- Input and change profile data
- Certify the profile for accuracy
- Input and submit a 5300 Call Report

Credit Union User

A credit union may or may not have any users with this role. Credit union users have the ability to:

- Change their personal information
- Input and change profile data
- Certify the profile for accuracy
- Input and submit a 5300 Call Report

Segregation of Duties

Information providers and sources

- Lending, Collections, Accounting, and IT

Preparers

- Accounting Manager, Assistant Controller, or Controller

Reviewers

- Controller or CFO

Authorized release

- CFO

Other Internal Control Considerations

Documentation and organization of data, the ability to recreate the report from retained support

Build or establish operational efficiency to eliminate waste and error :

- information gathering
- scheduling and completion
- use of data imports, templates, and roll forwards

Other Internal Control Considerations

Build in edit checks, statistical, and reasonableness proofs

Assign responsibility and train/cross train

Review and document responses to call report warnings generated by the Online 5300 Call Report system

Critical Areas & Common Mistakes

Loans held-for-sale not segmented from the rest of the loan portfolio (account code #003)

Foreclosed and repossessed assets are not reduced to the lower of cost or fair value less costs to sell and reclassified to other assets (#798)

Full-recourse loan participations should be classified as other assets, rather than loans or investments (#009)

Critical Areas & Common Mistakes

Negative shares are not reclassified to all other unsecured loans/lines of credit on page 2 (#644)

ATM, debit and credit card income, and expenses are improperly netted (page 5)

Loan delinquency is not adjusted for foreclosed and repossessed assets (pages 7 & 8)

Critical Areas & Common Mistakes

Loan charge-off and recovery information does not agree to the general ledger or the allowance for loan loss (ALL) calculation (page 9)

Total loan charge-offs do not agree with those approved by the board of directors (#550)

Unfunded loan commitments include the total line of credit amount (the outstanding loan balance is not deducted – page 10)

Critical Areas & Common Mistakes

An amount has not been disclosed for Overdraft Protection Program Commitments (#822)

- Even if there is not a specific program and no specific amount is committed to the member, “NCUA Rules and Regulations 701.21c.3. requires credit unions to establish a cap on the total dollar amount of all overdrafts the credit union will honor.
- Credit unions should report their cap amount minus any outstanding advances.”

Critical Areas & Common Mistakes

Mortgage loans approved but not funded are not reported as part of other unfunded commitments (#816)

The line of credit information does not match statements received from corporate credit unions, Federal Home Loan Bank, and other financial institutions (page 10)

Real estate loans sold but serviced by the credit union only includes residential real estate loans (#779A)

Critical Areas & Common Mistakes

Real estate loans sold but serviced by the credit union does not include loan participations sold (#779A)

The credit union reported real estate loans sold and serviced, but did not record mortgage servicing rights (#779)

The credit union did not complete Schedule A, Section 5 – TDR Loans (page 16)

TDR loans include all modified loans (page 16)

Use of Call Reports by Federal & State Examiners

Focus on monitoring call reports and reacting timely to potential problems, issues, or significant changes

Federal and state examiners request that credit unions maintain call report supporting documentation and that this be provided during the examination process

Examiners are thoroughly testing and validating call report disclosures, with no regard to materiality

Use of Call Reports by External Audit Firms

Misconception: the call report is audited during the financial statement audit process

Engagement acceptance and continuance process

- Determine risk level and pricing of engagement

Planning analytics and risk assessment process

- Determine significant risk areas and other areas on which to focus audit procedures

Validation of reports and schedules provided

Peer comparisons for exit meetings

Outside Party Considerations

- **Is the credit union profitable?**
- **Is the credit union well-capitalized?**
- **Does the credit union have any majority-owned CUSOs that require consolidation?**
- **What is the size and composition of the investment and loan portfolios?**
- **Does the allowance for loan losses (ALL) appear adequate based on the size and composition of the loan portfolio, delinquencies, charge-offs, and recoveries?**

Outside Party Considerations

Does the credit union have significant foreclosed and repossessed assets?

Does the credit union have intangible assets, goodwill or equity acquired in merger?

What unfunded commitments does the credit union have and are these reasonable in relation to the size and composition of the loan portfolio?

Does the credit union have ample sources of liquidity through available lines of credit?

Outside Party Considerations

If the credit union retains the servicing on real estate loans sold are mortgage servicing rights reported and are they reasonable in relation to the outstanding loan balance serviced?

Has the credit union been involved in the purchase or sale of loan participations?

Does the credit union have a member business loan portfolio? Does this represent a significant concentration risk?

Does the credit union have a significant amount of TDR activity?

Other Items to Consider

Document retention – NCUA regulatory requirements

Part 749 of the NCUA Rules and Regulations requires credit unions to keep either a hard copy or an electronic copy in their permanent records

Maintain supporting documentation to assist outside parties (at a minimum until the call report has been reviewed and validated by examiners and auditors)

Audit Considerations

Determine that access to the Credit Union Online system is properly limited and only available to authorized employees

Determine whether management has established effective internal controls over the call reporting process (segregation of duties)

Assess the following related to supporting documentation

- Adequate information
- Accurate

Audit Considerations

Verify that management reviews and documents responses to call report warnings generated by the Online 5300 Call Report system

Verify that management appropriately responds to all call report findings and recommendations identified in internal and external audit and regulatory examination reports

Determine how management addresses any passed or recorded audit adjustments identified by the external auditor

Audit Considerations

Test call report amounts and disclosures by tracing to supporting documentation

Determine whether the credit union properly completed consolidation of any CUSOs

Assess the consistency between call reporting, internal financial reporting, and audited financial statements

Assess management's process to monitoring new requirements, trends, and proposed regulations

Audit Considerations - Validation of Reports

Loans outstanding to credit union officials and senior executive staff (page 2)

Members' equity account activity and ending balances (page 4)

Net income/loss activity (page 5)

Loan credit quality disclosure information:

- Delinquency by loan class (page 7 & 8)
- Charge-offs and recoveries by loan segment (page 9)
- TDR loans (page 16)

Audit Considerations - Validation of Reports

Unfunded loan commitments (page 10)

Lines of credit (page 10)

Net worth calculation and ratio (page 11)

Risk-based net worth requirement (page 12)

**Nontraditional first mortgage loans
(balloon/hybrid loans – page 13)**

**Real estate loans sold and serviced by the credit union
(page 14)**

Resources

Link to Credit Union Online, including frequently asked questions, forms, and instructions:

<http://www.ncua.gov/DataApps/CUOnline/Pages/default.aspx>

Link to access call reports through Credit Union Online:

<http://cuonline.ncua.gov/CreditUnionOnline/CU/FindCreditUnions.aspx>

Questions?

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